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The Manufacturers Hanover

Financial Digest

Weekly Commentary, Selected Financial Data, and Business Indicators

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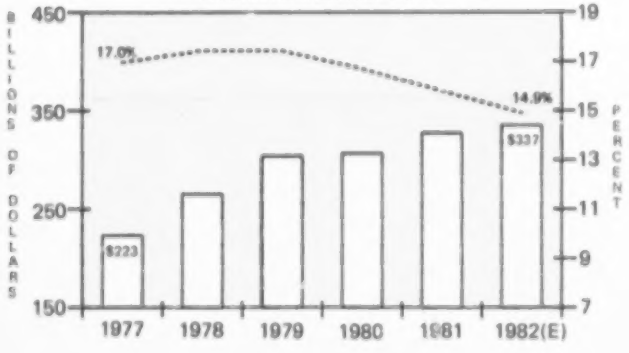
The Consumer . . .

As spring pushes its way north, prospects for a vigorous April economic rebound are vanishing just about as quickly as the residual winter snow. Among the more recent signs that business conditions remain soggy and the economy mired in recession were the renewed decline in retail sales in March and the tiny rise in consumer installment debt outstanding in February. Not surprisingly, with the rate of unemployment soaring toward a postwar high, consumer confidence in the economic outlook has plunged to new lows causing households to pull in their horns and trim their spending plans (Financial Digest—April 12, 1982). While indicative of the broader economy-wide malaise which still persists, the travail of the nation's merchants should not, however, be allowed to mask the very substantial improvements in the strength of household finances which are now underway—and which should ultimately lead to an upturn in consumer spending.

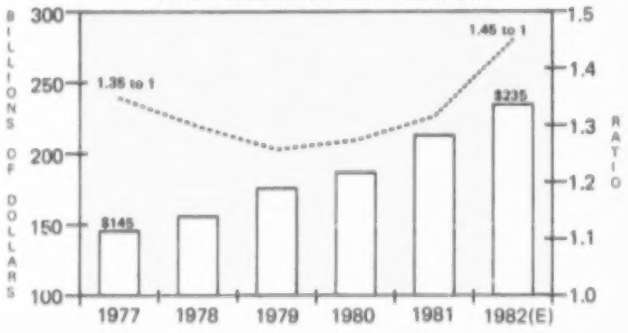
According to the Commerce Department, sales at the nation's retail establishments, after adjustment for seasonality but not for inflation, resumed their

CHART I
CONSUMER INSTALLMENT DEBT OUTSTANDING (BAR) VS. INSTALLMENT DEBT LIQUIDATIONS AS % OF DISPOSABLE INCOME (DOT)



descent in March, falling 0.5 per cent month-over-month. This followed a sizable 2.6 per cent gain in February, largely a weather-related rebound from the extremely depressed January levels. Meanwhile, the Federal Reserve reported that consumer installment credit outstanding rose by only $75 million in February, about one-sixth the size of the $443 million gain posted the month before. Outstanding auto, credit card and mobile home debt all fell during the month; only debt associated with personal loans and home improvement credit showed any increase at all.

CHART II
CHANGE IN HOUSEHOLD LIQUID ASSETS (BAR) VS. RATIO OF TOTAL HOUSEHOLD LIQUID ASSETS TO TOTAL HOUSEHOLD LIABILITIES (DOT)



Superficially, these reports suggest that consumers remain unwilling to boost spending substantially in the face of deteriorating economic conditions. But perhaps more important is what they don't suggest, namely, that the consumer is unable to step up household purchases, as well. The softening of credit-assisted retail purchases in general, and auto sales in particular, has caused a pronounced slowing in the use of credit. For example, installment debt outstanding increased, on average, by less than $850 million per month between August, 1981 and February, 1982, almost 20 per cent below the average monthly rate of rise posted during the same period one year earlier. But even more striking is the fact that during these past six months, installment debt was acquired at a rate almost 65 per cent below the average monthly rise registered during the immediately preceding, February-August six-month period.

. . . Appears Able . . .

This cautious use of installment debt and still sizable disposable income gains have produced a noticeable strengthening of consumer finances in recent months—reversing the earlier deterioration of

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the traditional indicators of household financial health. One such measure, the ratio of installment debt outstanding to disposable incomes, averaged just about 15½ per cent during the first two months of 1982, its lowest level since early 1977, and well below the almost 18 per cent peak reached in the fall of 1979.

Not only has the overall size of consumer debt diminished in relative importance, so, too, has the repayment burden associated with this debt. Whereas installment debt repayments had been absorbing close to 18½ per cent of disposable income in the spring of 1979, by early 1982, despite the jump in consumer lending rates, only about 15 per cent of take-home pay had to be set aside to service installment debt.

Indeed, the debt service burden has fallen so much in recent months that a smaller proportion of take-home pay is now being used to service existing installment debt than at the bottom of the 1973-75 recession. At that time, despite sharp spending cutbacks by households, installment debt repayments were still absorbing approximately 15½ per cent of disposable income. As a result, when looking at installment debt alone, the capacity of households to step up spending, especially credit-assisted spending for such goods as autos and appliances, may actually be greater now than prior to the

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit	4/7/82		
U.S. Gov'ts and Agencies Owned Outright & RPs	133.660	+ .209	+ 6.542
Loans to Depository Inst.	1.479	– .174	+ .592
Float	3.027	+ .972	+ .082
Total Reserve Bank Credit	147.465	+ 1.065	+ 6.415
Treasury Deposits with Federal Reserve Banks	3.938	+ .841	+ 1.075
Currency Outside Banks	126.898	+ .916	+ 6.219
Member Bank Reserves:			
Required	38.169	– .677	– .756
Excess (Deficiency)	.326	– .118	+ .189
Total Reserves Held	38.495	– .795	– .567
Net Borrowed Reserves	.987	– .022	+ .399
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	92.832	+ .007	– 7.206

Monetary Aggregates†		% Change Since Three Months Ago*	% Change Since Year Ago
M1	453.6	+ 5.8‡	+ 5.1‡
M2 (March '82)	1,864.0	+ 9.1	+ 9.6
M3 (March '82)	2,234.9	+ 8.6	+ 10.4
L (December '81)	2,643.3	+ 10.3	+ 11.5

†Seasonally adjusted. *Seasonally adjusted annual rate. ‡Four-week moving average.

New York Money Market

Offering Rates 4/16/82	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	12.75%	12.95%	12.60%
* Federal Agencies	14.40	14.20	14.30
* Project Notes—Taxfree (46% Taxable Equivalent)	13.52	14.63	NA
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	14.75	14.70	15.30

‡Finance Company Paper—Prime	
5- 14 days	14.88%
15- 29 days	14.38
30- 59 days	14.63
60- 89 days	14.25
90-179 days	14.13
180-239 days	13.50
240-270 days	13.50

‡* Bankers' Acceptances	
May	14.55%
Jun.	14.35
Jul.	14.15
Aug.	14.05
Sep.	14.00
Oct.	13.65

‡Industrial Paper—Prime	
30- 89 days	14.75%
90-120 days	14.38

†Federal Funds Effective Rate 15.25%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	4th Q'81	$ 2,998	$ 2,965	$ 2,731
Gross National Product (1972 Dollars)*	4th Q'81	$ 1,498	$ 1,516	$ 1,486
Percent Change, Annual Rate	4th Q'81	– 4.5	1.4	3.8
Change in Consumer Prices (all urban consumers)*	Feb '82	2.4%	3.6%	12.0%
Change in Producer Prices*	Mar '82	– 1.2%	– 1.2%	13.2%
Civilian Employment (Thousands of Persons)†	Mar '82	99,492	99,590	100,406
Unemployment as % of Civilian Labor Force†	Mar '82	9.0%	8.8%	7.3%
Personal Income*	Feb '82	$ 2,510	$ 2,498	$ 2,318
Leading Indicators Composite Index (1967=100)†	Feb '82	124.9	125.3	134.2
Industrial Production Index (1967=100) †	Mar '82n	141.2	142.3	152.1
Net Change in Consumer Installment Credit†	Feb '82n	$ 0.08	$ 0.44	$ 1.85
U.S. Merchandise Trade Balance †	Feb '82	–$ 0.39	–$ 4.09	–$ 2.13
Plant and Equipment Expenditures*	2nd Q'82	$336.77(a)	$345.46(a)	$316.73
Private Housing Starts (Thousands of Units)*	Mar '82n	947	924	1,318
New Construction Expenditures*	Feb '82	$ 230.4	$ 232.7	$ 254.5
Total Business Inventories†	Feb '82n	$ 509.0	$ 511.1	$ 484.1
Total Business Sales†	Feb '82n	$ 344.0	$ 336.7	$ 350.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. a-Anticipated.

recovery from the 1973-75 recession. (See Chart I on page 1.)

. . . But Not Yet Willing . . .

Of course, installment debt alone does not present a complete picture of household indebtedness. To this must be added mortgage debt. Here, too, the use of debt has slowed drastically, in this case, because of the virtual collapse of the housing market. With housing starts barely exceeding one million units in 1981, and existing home sales moribund, mortgage debt outstanding on one-to-four family homes increased by only six per cent last year—the smallest annual rise since the late 1960s. And with mortgage interest rates remaining at prohibitive levels and home prices only slowly drifting lower, mortgage debt acquisition is likely to remain subdued for some time. This, in turn, will probably ensure that total household liabilities expand only very slowly again in 1982. They increased by eight per cent in 1981, well below the average double-digit rates of rise recorded during the preceding ten years.

But consumers have been strengthening not only the liability side of their balance sheets. They have paid equal attention to the asset side, adding substantially to their financial reserves. Paced by a surge in money market fund shares, household liquid assets (defined as cash, savings accounts, money market funds and Treasury securities)

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Negotiable Time CD's Weekly Reporting Banks			
Nationwide (3/31/82)	133,186	– 1,219	+23,384
New York City (3/31/82)	32,868	– 1,036	+ 5,510
Commercial Paper (3/31/82)	166,138	– 3,870	+35,293

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (3/31/82)	202,624	+ 2,588	+29,429
New York City (3/31/82)	56,561	+ 1,189	+ 5,535

Total Loans Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (3/31/82)	476,419	+ 4,790	+45,588
New York City (3/31/82)	111,383	+ 2,688	+ 8,044

Financial Markets

	Friday 4/16/82	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	13.35%	– .16	– .35
180-Day Bills†	13.98	– .01	+ .53
Longest Bills†	14.13	+ .12	+ 1.25
Recent Issues:			
14¹/₈s 3/31/84	14.35	+ .16	
14s 3/31/86	14.08	– .02	
14⅝s 2/15/92	13.78	– .12	
14s 11/15/11	13.20	– .16	
Municipals:			
Bond Buyer–20 Bond Index* (4/15/82)	12.54%	– .45	+ 1.84
Blue List Total ($ Million)	$ 708	– $ 17	– $119
30-Day Visible Supply ($ Million)	$2,032	+ $167	– $746
Total	$2,740	+ $150	– $865
Corporates:			
Moody's Aa Composite (4/15/82)	14.89%	– .26	+ .56
30-Day Visible Supply ($ Million) ‡	$1,848	–$1,247	NA
Stocks:			
Dow-Jones Averages:			
Industrials	843.42	+ .48	– 162.16
Transportation	346.57	– 2.27	– 100.81
Utilities	112.27	+ 1.75	+ 5.11
65 Stocks	332.97	+ .30	– 60.19
Standard and Poor's 500 Stocks	116.81	+ .59	– 17.89
N.Y.S.E. Composite Index	67.26	+ .37	– 10.50
N.Y.S.E. Avg. Daily Vol. for Week (000's)	48,438	– 4,254	– 3,457

* 46% Taxable equivalent 23.22%. † Bond equivalent.
‡ Series redefined: Historical data not available.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 4/16/82	Week Ago
Overnight	15.75%	15.00%
1 month	15.50	15.56
3 month	15.50	15.56
6 month	15.50	15.63
1 year	15.19	15.38
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	14.75%	14.80%
Long Term (7 to 15 yrs.)	14.85	14.90

FOREIGN EXCHANGE SPOT RATES

New York Opening (4/16/82)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02181	45.85
Canada	.8180	1.2225
Denmark	.1217	8.2150
France	.1585	6.3105
Germany	.4120	2.4270
Italy	.0007495	1334.20
Japan	.004033	247.95
Mexico	.02176	45.96
Netherlands	.3714	2.6925
Switzerland	.5044	1.9825
U.K.	1.7555	.5696

posted a strong gain in 1981—and now stand at record high levels, whether looked at in current dollars or after adjustment for inflation. What is more, with their growth currently running well ahead of that of household debt, liquid assets alone may soon exceed total household liabilities by almost 50 per cent. (See Chart II on page 1.)

. . . To End This Recession

With debt burdens trimmed and short-term financial assets soaring, the consumer now appears in a good position to shrug off the negative effects of slumping bond, equity and home prices. But, in any event, the dampening impact of these factors on spending may have been exaggerated. In the case of bonds, for example, the buying habits of many long-term investors are likely to be little affected by fluctuations in the market value of their bond holdings, as long as the flow of interest income from these securities is uninterrupted. Barring borrower default, these payments continue irrespective of fluctuations in the market value of the fixed income portfolio.

Even the downturn in equities prices, which should have a more immediate impact on spending decisions since they are more widely held by the public, may have been unduly emphasized. The share of total household investments devoted to corporate equities as diminished sharply over time—from more than 50 per cent in the late 1960s, to 30 per cent by the end of 1981.

Although the value of bond and equity holdings may be diminished, with the rate of inflation moderating, future disposable income gains will buoy consumer buying power even more than in the past. What is more, the recent improvements in household finances allow significant leeway for stepped-up spending. For example, simply lifting the installment debt outstanding-to-disposable income ratio back into the 17 to 18 per cent range could boost retail sales by at least $40 billion. If half of that was devoted to auto sales, some two million new automobile sales would occur at prevailing prices. The ability to spend is there, but is the will?

The Manufacturers Hanover track record in Fixed Income Management spells "performance."

For the period 1972-1981, the MH Fixed Income Fund delivered far greater returns than the Salomon Bros. Index and the P.I.P.E.R. Median.

The reason: The Manufacturers Hanover approach to investment management. You see, we believe in *active* management.

This approach allows us to choose from a variety of innovative products to take advantage of prevailing market conditions while keeping a client's investment objectives firmly in mind.

For example, Manufacturers Hanover went beyond the concept of bond immunization to that of contingent immunization. This allows our portfolio managers to actively trade bonds, as long as the overall rate of return remains above a predetermined "floor." If the return hits the "floor," the portfolio is immunized to lock in the original targeted yield.

While contingent immunization does not guarantee the return, long term simulation, historic analyses and Manufacturers Hanover's actual experience indicate a likelihood of maintaining the floor with a high degree of probability.

It is this experience, combined with our investment philosophy, that has enabled us to outperform the averages. Just look at our ten year performance.

To learn how the Manufacturers Hanover active approach to pension fund management can affect your plan, contact William C. Petty, III, Vice President, at (212) 957-0760. Or write to him at the address below.

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*These numbers are annual time-weighted rates of return for the ten year period ending December 31, 1981.
†Pension and Investments Performance Evaluation Report - Pooled Fixed Income Funds of Banks and Insurance Companies